IN THE

# Supreme Court of the United States

October Term, 1942.

No. 497.

A. M. ANDERSON, Receiver of the National Bank of Kentucky, - - Petitioner-Appellant,

*versus*

KATHERINE KIRKPATRICK ABBOTT, Administratrix of the Estate of David J. Abbott, Deceased, ~~Et Al.~~, - - - Appellees.

SUSIE E. TELLMAN, Et Al., - Cross-Appellants,

*versus*

A. M. ANDERSON, Receiver of the National Bank of Kentucky, - - - Cross-Appellee.

## BRIEF FOR APPELLEES AND CROSS-APPELLANTS, SUSIE E. TELLMAN, EMMA BISCHOFF, AND OTHER CLASS B DEFENDANTS SIMILARLY SITUATED.

HENRY M. JOHNSON,
*Attorney for Susie E. Tellman, Et Al., Class B Defendants.*

WESTERFIELD-BONTE CO., INCORPORATED, LOUISVILLE, KY.

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holders of National Bank of Kentucky "*evolved the scheme*" of Banco, and *mislabeled* the stock "*non-assessable*," through which they were "*plainly* and *intentionally* attempting to *evade*" the United States Statutes; that by reason thereof they are "*not entitled*" "in *equity* and *good conscience* thus to *shield* themselves" by Banco.

The law of "equity and good conscience," so correctly invoked by the Receiver in this case, entitles Class B Stockholders and defendants, who lost money to the Bank, which used the said money for the Bank's purposes, to participate like the Bank's other creditors in the Bank's assets.

Oppenheimer v. Harriman National Bank and Trust Company and Conservator of Harriman Bank and Trust Company (1937), 301 U. S. 206, 81 L. Ed. 1042, 57 S. Ct. 719.

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**BRIEF FOR APPELLEES AND CROSS-APPELLANTS, SUSIE E. TELLMAN, EMMA BISCHOFF, AND OTHER CLASS B DEFENDANTS SIMILARLY SITUATED.**

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*May it please the Court:*

## STATEMENT OF THE CASE.

This Court recently entered an order herein giving to Mrs. Susie E. Tellman, *et al.*, cross-appellants in the lower Court, who paid for part of the record there, and

which was brought up to this Court, the right to file this their brief herein.

If this Court should affirm the judgment of the 6th Circuit Court of Appeals, then this brief can be disregarded. If, however, this Court reverses the lower Court and holds that Banco was, as Receiver alleged in his bill and contended during the trial, and thus concludes in his brief (p. 62) "unlawful" a "corporate instrumentality of the shareholders" of National Bank of Kentucky—"organized to support a failing National bank"—"never qualified" to do business in Kentucky, and "expressly forbidden by Kentucky law," etc., etc., then the innocent Class B stockholders, who bought stock in said outlaw corporation and agency of the Bank, have a just claim for the return of their money paid into Banco and used by the Bank for its own purposes, and for furthering its own ends.

## BRIEF OF THE ARGUMENT.

**1. There Would Result a Paradox if Receiver Would Be Permitted to Recover Herein From Stockholders of Banco on the Ground of Banco's Illegality, and if, at the Same Time, Innocent Class B Stockholders, Would Not Be Permitted to Recover on the Same Ground the Money They Put Into Banco.**

If Banco, by reason of the alleged illegality and constructive fraud, etc., did not come into sufficient and substantial existence, as to legality, so as to insulate its promoters, it also did not come into a sufficient and substantial existence, as to legality, so as to support a sale of its stock to innocent purchasers, upon the inconsistent hypothesis that it was a legal "honest to goodness" independent substantial corporate entity.

If Banco was a fraudulent or sham or masquerade corporate device, as the Receiver charges it to have been, in order to enable the Bank to engage in unlawful acts, surely Banco could not at the same time be so substantial and virtuous as to be the basis of taking money from innocent and duped outsiders to whom its fraudulent stock was sold.

Without, of course, casting any personal aspersions on the Receiver, whose integrity and diligence are unquestioned, yet we respectfully submit that the Receiver attempts herein to blow both hot and cold. He desires Banco to be meat for him, yet poison for others. He characterizes Banco as unspeakably foul, then in the same breath he attempts to embrace it to his bosom. He condemns Banco in unmeasured terms, only to immediately thereafter seek to use and appropriate it for his own advantage. He discards Banco as a counterfeit, then tries to pass it off on others as genuine and thereby seeks to profit from it. The law does not permit any legal magician, by the mere wave of a magic wand, to thus accomplish such an impossible feat and to thus wreak deadly havoc upon thousands of innocent purchasers of Banco stock. "Consistency, thou art a jewel."

## 2. "Equity and Good Conscience"—the Yardstick in This Case.

The Receiver has properly invoked *equity*, in this case, to quote from his Bill, for "winding up the affairs" of the Bank (R. 57). He appropriately asks for a decree in accordance with "equity and good conscience," which he repeats in his Bill (R. 69), and Prayer (R. 74). Anything short of this position by the Receiver would have been inconsistent with the law and the faithful Receiver he has been.

The particular "occurrence or transaction," which the Receiver asks the Court to examine and make a decree concerning is the legal status of those who held stock in the corporation—BancoKentucky.

It is fundamental that equity once taking jurisdiction will not stop at part-way measures, but will do absolute, full and complete justice to all the parties, even though the Court may have to do so on its own initiative.

## 3. The Equities in the Case, If the Receiver's Charges Should Be Upheld.

If, as the Receiver charges, Banco was the illegal and constructively fraudulent (R. I. 220) agency and instrumentality of the National Bank of Kentucky and its organizing officers, then "equity and good conscience" requires that this Court of Equity recognize that the nearly 3,000 Banco stockholder defendants herein fall into two classes, viz.:

Class A—Promoters, organizers, planners and launchers of Banco, made up of National Bank of Kentucky's officers, directors and stockholders, who held 95% of the Bank Stock, and who exchanged their Bank Stock into Banco Stock, and who retained and exercised absolute dominion over Banco.

Class B—Purchasers for cash of Banco Stock, made up of the outside public, who had nothing to do with the organizing of Banco, and who did not own any National Bank of Kentucky Stock, and who did not exchange any of said Bank Stock for Banco Stock, and none of whose money, which was paid for Banco Stock, ever went to buy any of the National Bank of Kentucky Stock (for Banco never purchased a share of National Bank of Kentucky Stock), and who had nothing to do with the management and operation of Banco.

and that, in administering "equity and good conscience," this Court should adjudge that, under the facts and circumstances of this case, Class B defendants have equities, which entitle them herein to affirmative relief, viz., the recovery of the money they were induced to invest in this legally condemned corporation (in the event this Court should hold it to have been such a corporation).

### 4. Statement as to Susie E. Tellman, Emma Bischoff Et Al., of Class B Group of Defendants.

The record shows that Susie Tellman, Emma Bischoff and P. A. Gaertner belong to Class B stockholders; that neither of them owned any National Bank of Kentucky Stock, nor any Trustees Participation Certificates in Bank Stock, which were exchanged into Banco Stock; that they bought their Banco Stock for cash, and that they were not the promoters, organizers, planners or launchers of Banco, and had nothing whatever to do with its management or operation.

Mrs. Susie E. Tellman is a housewife and Emma Bischoff, who died since this action was filed, was a stenographer and clerk, each of whom invested their savings of $2,500.00 cash in Banco Stock. As "Miss Emma" was for many years the stenographer of one of the writers of this brief (in fact the first one he had when he was admitted to the bar), it can be seen that his real personal interest was easily enlisted for her and for those in similar position with her.

When this action was filed against Tellman and Bischoff and others, for approximately $232.00, with interest, against each of them, and against other of the Class B stockholders, for comparatively small amounts, it was apparent that the record would be so voluminous and expensive as to be absolutely prohibitive for Tellman, *et al.*, Class B Stockholders, to employ and adequately pay counsel to perform the necessary work involved for a full and complete investigation into the affairs of Banco, in the stock of which these persons

had been induced to invest. When we, therefore, were besought by Tellman and Bischoff to protect their interests as best we could, we recognized that about all we could do would be to merely watch the proceedings, which were to be so voluminous and expensive, and then, in a more or less general way, point out to the Court the equities, which were developed in the record in favor of these Class B defendants, and pass up to the Court the task of working out "equity and good conscience" to them. It is out of this approach and relationship that we respectfully write this brief, believing that the record is such as to cause the Court to decree that such equities exist herein in favor of the Class B defendants as to entitle Class B defendants to affirmative relief in the event any recovery is decreed herein for the Receiver.

### 5. Equities and Claims, Applicable to One Defendant Herein Are Applicable to All Similarly Situated.

In this case, with several thousand defendants, the case was practiced below in accordance with the following portion of the lower Court's order of October 31, 1939:

> "All pleadings and motions heretofore filed by any defendant, which relate to the merits of the case in general and not to some special fact or decision applicable to the particular defendant filing such pleadings, shall inure to the benefit of all defendants."

**6. Claims and Counterclaims of Defendants Against the Bank, Growing Out of the Transaction Involved in the Action Are To Be Adjudicated by the Court, and If Allowed, a Pro Rata Distribution of Assets in Receiver's Hands Is To Be Made to Such Claimants, Along With Claimants Who Were Depositors in the Bank.**

When this action was filed in February, 1936, the above proposition of law was unsettled, but later on, April 26, 1937, the Supreme Court of the United States rendered a decision in a bank receivership case, in which the Supreme Court held that a person, who had bought stock through misrepresentations of the bank's affiliate, had a just claim against the Receiver of the bank, which claim would participate on a pro rata basis with other claimants basing their claim upon money on deposit in the bank at the time it closed. This was the case of Oppenheimer v. Harriman National Bank & Trust Company and Conservator of Harriman Bank and Trust Company, 301 U. S. 206, 81 L. Ed. 1042; 57 S. Ct. 719, decided April 26, 1937. This Court has had occasion to follow the above Supreme Court decision on the procedural or jurisdictional question in a very recent case of Lucking v. Schram (1941), 117 F. (2d) 160, affirming Schram v. Lucking (1940), Eastern District of Michigan, 31 F. Supp. 749. The lower Court said:

> "Admittedly in the Oppenheimer case there was payment of the assessment before suit against the Bank was instituted but the decision does not

determine that two suits were necessary, and the trend of new rules and Courts in general is to discourage separate actions tending towards multiplicity of suits and is now rather partial towards combining in one litigation, wherever possible, for determination, the rights of all parties in one action in one subject matter or arising out of one transaction. This is not only the spirit of Rule 13, but it is also the spirit and intention of Rule 14, where extra parties who might be affected by or have some rights in the litigation are permitted to be joined and brought into the same action, even where jurisdictionally they could not originally have been made defendants in Federal Court. * * * The parties being present, this Court determined that the only logical and sensible thing to do was to proceed with a hearing on the merits of defendant's counterclaim. * * *. This court can see no logic in compelling defendants to start a separate action against plaintiff when plaintiff has already brought them into court."

This case was affirmed in 117 F. (2d) 160 (1941), by the Sixth Circuit Court of Appeals. However, the counterclaim was held to be illegal in a decision upon its merits. The counterclaim in that case was not in any way similar to the counterclaim asserted herein by Banco's Class B Stockholders. In that case the counterclaim was attempted not by an innocent Class B Stockholder who had bought for cash his stock, but by a Class A Stockholder who had exchanged Bank Stock for the holding company stock, etc.

**7. If This Court Should Hold, After Considering the Great Mass of Testimony in This Case, that Receiver Has Made Out Its Case that Banco Was Illegal and Constructively Fraudulent, Then Innocent Class B Stockholders, Such as Tellman, Et Al., Have a Just Claim Against the Bank and Its Assets in the Hands of the Receiver, for Recovery for the Amount They Paid for Said Worthless Banco Stock.**

If Banco should be held to be the illegal, etc., entity, which—

1. Receiver charges in his Bill (R. I. 66-69);
2. Receiver charges in his request for Findings Nos. 16, 17, 18, 19, 20, 21 (R. I. 184-187) and Nos. 28, 30, 31, 32, 33, 34 (R. I. 192-195 and Nos. 57, 58 (R. I. 212) (R. I. 120);
3. Which Receiver charges in his Brief on this appeal, particularly in footnote on page 105 of Receiver's Brief,

then Tellman, *et al.*, Class B Stockholders, have a just claim against the Bank's assets for the money they paid for said worthless stock, which claim is based on the following:

1. That illegal Banco was organized and attempted to be launched by officers and directors of the National Bank of Kentucky, and thereafter was the Bank's child and agency, completely dominated and under the dominion of the Bank, which used Banco's assets for the Bank's own purposes.

2. The statement in Banco's Articles of Incorporation that "VIII, the private property of the stockholders shall not be subject to the payment of any corporate debts whatever."

3. The statement on Banco's Certificates of Stock that the Stock was "full paid and non-assessable."

**8. The Above Statements Constituted Misrepresenting and Misbranding of the Article Sold, Measured by the Legal Yardstick, Well Set Out as Follows.**

"Goods are misbranded if they bear any statement which will deceive or mislead any purchasers who are of normal capacity and who use that capacity in a common sense way."

United States v. Two Cases of Chloro-Naphtholeum Disinfectant, 217 Fed. 477, 484.

That the above were material statements of fact, not only admitted but charged by the Receiver in Paragraph XVI of his Bill (R. I. 68-69), is seen from the following portion of Receiver's Bill:

"The holders of the Trustees Participation Certificates who organized the BancoKentucky Company as a holding corporation for their bank stock, *well knowing* that said bank stock was subject to the individual liability of shareholders of national banks, imposed by the Acts of Congress, Sections 5151 and 5234 of the Revised Statutes of the United States and knowing that Bank stock of state banking institutions was subject to individual liability imposed by state laws, nevertheless, in the organ-

ization of the said BancoKentucky Company, intentionally undertook to evade the provisions of said sections of the Acts of Congress by deliberately omitting from the Articles of Incorporation any provision for the payment of the liability upon national and state bank stocks provided by the laws of the United States, the Commonwealth of Kentucky and other states, and *deliberately* and *intentionally* sought to evade said liability by including the Articles of Incorporation of Banco-Kentucky Company the following language:

> 'VIII. *The private property of the stockholders shall not be subject to the payment of corporate debts to any extent whatever,'*

and by printing in its certificates of stock the words 'full-paid and non-assessable,' and in so attempting to evade such assessment liability perpetrated a fraud upon the depositors and creditors of the National Bank of Kentucky for whose benefit this action is brought."

Also in the opening statement before the trial, by Judge Marx, for the Receiver, we find the Receiver laying great stress on these "misrepresentations" in the following (R. II, 8):

> "Mr. Marx: Well, that is what they did. Now, how did they do it? They undertook to organize a general corporation under the laws of the State of Delaware, and almost the first article that they wrote into that corporation charter was—these men sitting as bank directors, these men who were the shareholders of that bank, these men who knew that they were subject to dou-

ble liability, wrote into that article of incorporation, 'The personal property of the shareholders thereof shall be exempt from the payment of its debts,' and then, on top of that, they caused stock certificates in the company to be printed, and put on the face of them '*fully paid and non-assessable*.'"

Throughout the taking of evidence and all through the trial the Court will see how the Receiver laid emphasis on the above statements in Banco's Articles of Incorporation and Certificates of Stock.

If these "misstatements" and "misrepresentations" can be any basis of Receiver's claim against Class A defendants, surely they are equally sufficient in "equity and good conscience" as a basis of Class B defendant's claim to remedy the wrong done them.

**9. The Receipt of Banco Dividends Has No Adverse Effect on the Right of Class B Stockholders to Recover Out of Bank Assets, Except Probably to Give Credits for Dividends Received.**

Receiver's counsel attempt to fasten the double liability, applying to Bank stock, upon Class B stockholders of Banco, upon the ground that these stockholders received some dividends on Banco stock, and that some of the money, which paid these dividends could be traced as having come from dividends, which Banco received on the National Bank of Kentucky stock. Receiver's counsel argue that these stockholders knew, or should have known, the source from

which their dividends came, and that as a result, this fastens double liability upon the stockholders, in spite of the fact that the said stockholders themselves, never owned a share of stock of the said Bank; and that not a cent of money, which they paid into Banco, was ever used by Banco to buy a single share of stock in said Bank.

The only possible effect the receipt of such dividends could have upon a stockholder so receiving them, would be to make such stockholder liable for a return of any dividends illegally declared. Receiver's counsel do not contend that the dividends were illegally declared, and do not ask for any return based upon any such alleged illegal declaring of same. They merely attempt, through some species of reasoning, to contend that the receipt of such dividends, which were small, would have the effect of making the recipients liable not for the dividends, but doubly liable for Bank stock, which the recipients never owned, and for which none of their money ever went to buy.

That the Receiver is wrong in this contention is seen by the opinion of the United States Circuit Court of Appeals for the Fourth Circuit, in the case decided on January 9, 1939, Nettles v. Childs, 100 F. (2d) 952, which case was a sequel to the case of Nettles v. Rhett, cited by the Receiver. In the Childs case, *supra*, the Court said:

> "Four semi-annual dividends of 3¼% each were paid the preferred stock during 1930 and 1931. The payments were made out of funds re-

ceived by the holding company as dividends on the bank stock, which it held. The defendants in the pending case, however, had no knowledge at the time of the receipt of these dividends that the earnings of the company were derived from bank stock, and did not suspect that such was the case until after the failure of the company."

The Court discarded the contention that the receipt of such dividends fastens liability on stockholders of the holding company, saying:

"The acceptance of dividends by the defendants does not impair their defense. They had no knowledge of the illegal business of the holding company until long after the dividends were received; and without knowledge, there could be no ratification or acceptance on their part of the illegal acts of the corporation. The present suit does not seek a recovery of the amount of the dividends received, but a much greater sum equal to the par value of the shares as an extra statutory liability. It was held in McDonald v. Williams, 174 U. S. 397, 19 S. Ct. 743, 43 L. Ed. 1022, that dividends paid by a solvent national bank to a stockholder entirely out of capital are not recoverable if the stockholder receiving them acted in good faith. A federal statute, 12 U. S. C. A., §56, forbade any national bank during the continuance of its banking operations to withdraw or permit to be withdrawn in the form of dividends or otherwise, any portion of its capital; but the court held that a shareholder who in good faith receives a dividend paid out of capital could not be said to have participated in the withdrawal of capital."

Any point the Receiver might attempt to make that Class B stockholders of Banco must have known that the four dividends of 20c per share each which they received from Banco could be traced to dividends which Banco received from National Bank of Kentucky stock, is only an unjustifiable inference and assumption. No proof whatever shows this knowledge and it cannot be assumed. And even bare knowledge would not be sufficient in "equity and good conscience" to hold them doubly liable when not a cent of their money nor Banco's money ever went into National Bank of Kentucky Stock.

**10. The Finances of the Case Make Easily Possible the Working Out the Mechanics of Class B's Equities, Should Any Recovery for the Receiver Be Decreed Herein.**

It is indeed fortunate that should the Court hold the Receiver as entitled to any recovery herein, then there will be sufficient money to pay Class B defendants their pro rata distribution, as seen from the following facts and figures:

## THE AMOUNT PAID BY CLASS B DEFENDANTS WAS $5,397,500.00.

| | |
|---|---|
| Total amount paid in cash into Banco was (White, A. 373, p. 470) | $9,869,650 |
| Holders of Bank & Trust Co. participating certificates paid in cash for Banco stock ........................ (Shuck, p. 885) | 4,471,950 |
| Leaving amount put up by outside public or Class B defendants............ | $5,397,500 |

Class B defendants have valid and just claims against the Bank's assets for . .$5,397,500.00, which amount they invested in illegal Banco, a fraudulent and illegal Company, promoted and attempted to be launched by the Bank and its officers, directors and stockholders.

From this should be deducted four dividends of 20c per share, or a total dividend of $80.00 on each 100 shares of Banco stock, which was sold for $25.00, or a total of $2,500.00. These dividends totalling $80.00, on stock costing $2,500.00, means the total dividends paid are equivalent to 3.2 percent on the total cost.

| | |
|---|---|
| Total amount paid by Class B defendants ........................ | $5,397,500.00 |
| Less total dividends paid (equivalent of 3.2 percent on $5,397,500.00) . . . | 172,720.00 |
| Net amount due Class B defendants. . | $5,224,780.00 |

Class B defendants and claimants are entitled to participate in the distribution of the Bank's assets, and to receive a distribution dividend of 77 percent, the amount heretofore paid to other of Bank's creditors. This 77 percent distribution on $5,224,780.00 to Class B defendants would amount to................$4,023,080.00.

The total assessment against the Bank's stockholders was $4,000,000.00, with interest, approximating..........$6,160,000.00, which should be the total amount apportioned against Class A defendants.

The actual collection to be realized,
Figured at 90 percent would be......$5,444,000.00
Figured at 85 percent would be......$5,236,000.00
Figured at 80 percent would be......$4,928,000.00.

Only $4,023,080.00 is needed to make Class B claimants receive 77 percent and to be equal to other claimants, who have heretofore received 77 percent distribution. The balance remaining, after 77 percent distribution to Class B defendants and claimants, would be distributed to all of those to whom the Bank was under obligation, including Class B defendants.

**11. Tellman, Et Al., by Proper Pleadings in the Case, Invoked for Themselves and All Other Class B Defendants Similarly Situated, an Equitable Claim Against the Bank's Assets in the Hands of Receiver Along With Other Claims Against The Bank for Their Loss Occasioned by Purchase of Misrepresented and Misbranded Stock in Illegal Banco.**

These pleadings are an answer and amended answer, counterclaim and cross-action of Tellman, *et al.* (R. ~~158-168~~, Rec., Vol. 1), the latter of which was filed on November 1, 1938. After this filing, the Receiver did not make any effort to file any reply until November 15, 1939,—over a year later. In the meantime the case had stood for trial, in the spring of 1939, for an extended period of time and much testimony and proof had been taken and the taking of testimony closed. The case was then set for the fall, for briefs and final arguments. During the summer the Receiver and other defendants, as well as Tellman, *et al.*, filed and exchanged briefs with each other and the case was set to November 15, 1939, for oral arguments. On this late day the Receiver tendered and offered to file a Reply to Tellman's, *et al.*, pleading filed over a year before, to-wit, on November 1, 1938, to which filing Tellman objected, but the Court allowed the pleading to be filed. Tellman's counsel proceeded, however, to argue the case, addressing themselves to the points of law involved, rather than any points of fact, except the admitted ones, and the whole case was submitted.

The lower Court held that Banco was a legitimate corporate entity and dismissed Receiver's claim. It was, therefore, unnecessary for the lower Court to consider Tellman, *et al.* contention. This is also what happened in the Court of Appeals.

In Receiver's brief in the Court of Appeals, it was contended that Tellman, *et al.'s* claim was barred by limitation. To this Tellman, *et al.* answer that their claim grows out of the same transaction and subject-matter on which Receiver's claim is based, and the law is that so long as the main action by plaintiff is timely, then defendant's claim is not barred by limitation. This was specifically decided by the Supreme Court in Bull v. U. S. (1935), 295 U. S. 247, 79 L. Ed. 1421, wherein the Supreme Court, speaking unanimously, through Justice Roberts said that "such a defense is never barred by the Statute of Limitations so long as the main action itself is timely." See also Stone v. White (1937), 301 U. S. 532, 57 S. Ct. 851, and Aultman & Taylor v. Meade (1905), 121 Ky. 241, 89 S. W. 137.

We can conceive of the decision in this upper Court being such that it would be necessary to remand the case, leaving open the determination of certain questions by proof which the upper Court might direct the lower Court to take or have the Master take. In any event, we feel that as this case has been pending now for so many years, this Court should, on these appeals, consider all the questions of law raised by way of defense and counterclaim, so as to operate as a guide to the lower Court in the event this case should be reversed and remanded for "further proceedings," etc.

## RELIEF ASKED OF THIS COURT BY CLASS B DEFENDANTS.

Class B Stockholders and defendants respectively ask this Court, in the event it should hold that the Receiver is entitled to any recovery herein, to also hold that "equity and good conscience" entitles Class B defendants to a decision that the cross-appeal of Tellman, *et al.*, for Class B Stockholders, from so much of the judgment below as dismissed their counterclaim, be sustained on the following ground:

> That Class B Stockholders, on so much of their answer as amended, as was uncontroverted up until months after the evidence had all been taken in the case and the briefs prepared and exchanged, and the case was in the process of argument, have a claim against the assets of the National Bank of Kentucky, in the hands of the Receiver, from which assets they are entitled to a pro rata distribution, just like the other creditors of the Bank, for the amount of money which they invested in Banco, the illegal agency of the Bank, which money, through the Bank's officers dominated Banco, was appropriated for the Bank's use, and squandered in wild, illegal transactions.

## CONCLUSION.

The Receiver in no way "pulled his punches" in characterizing the *iniquity* of Banco. Receiver says, in his Brief (p. 62), that Banco was *"unlawful"* a "corporate *instrumentality* of the *shareholders"* of *National Bank of Kentucky*—*"organized* to support a *failing* National bank"—*"never qualified"* to do business in Kentucky, and *"expressly forbidden* by Kentucky law," etc., etc. (p. 28)—"a *creature* born out of

a *resolution adopted* by the Board of Directors of the *National Bank of Kentucky*"; that (p. 35) "its *stockholders* and their agents, the officers and directors, *are responsible*"; that the condition of the National Bank of Kentucky progressed from bad to worse through the following steps—(p. iii) "*unhealthy* on April 23, 1927" "*no improvements* in its condition during the next Six Months"—"*getting worse*" on March 9, 1928—"*very bad*" on October 13, 1928—when Banco was promoted and organized it was in a "*precarious* condition"; that (p. 6) "knowing" this condition the stockholders of *National Bank of Kentucky* "*evolved the scheme*" of Banco, and *mislabeled* the stock "*non-assessable*," through which they were "*plainly* and *intentionally* attempting to *evade*" the United States Statutes; that by reason thereof they are "*not entitled*" "*in equity* and *good conscience* thus to *shield* themselves" by Banco.

The law of "equity and good conscience," so correctly invoked by the Receiver in this case, entitles Class B Stockholders and defendants, who lost money to the Bank, which used the said money for the Bank's purposes, to participate like the Bank's other creditors in the Bank's assets, as decided in the recent case of the Supreme Court of the United States in Oppenheimer v. Harriman National Bank & Trust Company and Conservator of Harriman Bank and Trust Company, 301 U. S. 206, 81 L. Ed. 1042, 57 S. Ct. 719, decided April 26, 1937.

Respectfully submitted,

HENRY M. JOHNSON,

*Attorney for Susie Tellman, Emma Bischoff and other similarly situated Class B Defendants.*

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# SUPREME COURT OF THE UNITED STATES.

No. 3.—OCTOBER TERM, 1943.

A. M. Anderson, Receiver of National Bank of Kentucky, of Louisville, Petitioner,

*vs.*

Katherine Kirkpatrick Abbott, Administratrix with the Will Annexed of the Estate of David J. Abbott, Deceased, et al.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

[March 6, 1944.]

Mr. Justice DOUGLAS delivered the opinion of the Court.

The primary question in this case is whether on these facts shareholders of a bank-stock holding company are liable under § 23 of the Federal Reserve Act, 12 U. S. C. § 64, and § 12 of the National Bank Act, 12 U. S. C. § 63, for an assessment on shares of a national bank in the portfolio of the holding company.

The essential facts[1] may be briefly stated.

Banco Kentucky Company was organized under the laws of Delaware in July, 1929. It had broad charter powers in the field of finance. It was organized by the management of the National Bank of Kentucky and of the Louisville Trust Company—banking houses doing business at Louisville. Banco perfected the desired alliance between them by acquiring most of their shares[2] in exchange for its shares. The Bank, the Trust Company, and Banco each had the same directors and certain common officers. Some of the shareholders who made the exchange also purchased additional shares of Banco stock at $25 per share. Banco stock was also sold at that price on the market to those who did not

1 Further details concerning the financial transactions indirectly involved in this litigation may be found in Atherton v. Anderson, 86 F. 2d 518, 99 F. 2d 883; Banco Kentucky's Receiver v. Louisville Trust Co.'s Receiver, 263 Ky. 155.

2 The shares of the Bank and the Trust Company had been earlier transferred to trustees who issued Trustees' Participation Certificates. It was these certificates which Banco received from the shareholders of the two banks in exchange for its shares. The command which Banco had over the underlying shares is described in Laurent v. Anderson, 70 F. 2d 819.

own any shares in the Bank or the Trust Company. All told some $9,900,000 in cash was realized by Banco from the sale of its shares—about $6,000,000 of which was financed on loans from the Bank and from the Trust Company. Banco's stock certificates stated that the shares were "full-paid and non-assessable". Its certificate of incorporation provided that the stockholders' property should "not be subject to the payment of corporate debts to any extent whatever".

The closing date for the exchange of shares was September 19, 1929. Beginning about September 25, 1929, Banco acquired a majority stock interest in each of five banks in Kentucky and two banks in Ohio, and a minority stock interest in another bank in Kentucky. Of these eight banks, two were national. The shares of the state, as well as the national, banks in the group carried a double liability.[3] The price paid for the shares in these banks was about $11,500,000—of which some $6,500,000 was paid in cash and $5,000,000 in Banco's shares. Not all of Banco's funds were invested in bank shares. It acquired for $2,000,000 a $2,000,000 note of its president.[4] It purchased 625 shares of a life insurance company for $25,000 cash. It purchased and retired 106,000 of its own shares at a cost of over $2,300,000—some $275,000 less than Banco received for them. It received dividends of about $1,180,000 on the bank stocks owned by it and paid them out at once as dividends on its own shares. It borrowed $2,600,000 from a New York bank and paid back $1,000,000. With $600,000 of that loan it purchased from the Bank certain dubious assets[5]—a transaction which the Ken-

[3] See Ky. Rev. Stat. 1942, § 287.360; Ohio Code Ann. 1940, § 710-75. At or about the time of Banco's failure the shares in the other banks were sold or disposed of at rather nominal prices. It appears that the closing of the Bank was followed by heavy runs on these other banks; and the local interests in most of the cities where the banks were located were willing to support the banks to keep them open if Banco would surrender control. Banco, it seems, was also anxious to avoid double liability on those shares.

[4] The president of Banco was also president of the Bank. This note was acquired in November, 1929, from Wakefield & Co. It was secured by 60,000 shares of Banco stock and 22,500 shares of stock of Standard Oil of Kentucky. Nothing was ever paid on the note. Nothing was realised on the Banco stock. Some $440,000 was realized on the Standard Oil stock. In December 1930 the president of Banco and maker of the note filed a voluntary petition in bankruptcy. He was discharged. Wakefield & Co. made an assignment for the benefit of creditors in 1931 and apparently no dividends have yet been paid its creditors.

[5] These were a Murray Rubber note in the amount of $580,000 and a note of Lewis C. Humphrey for $20,000—of which the bank examiner had been quite critical for some time.

tucky court later set aside. *Banco Kentucky Co.* v. *National Bank of Ky.*, 281 Ky. 784. It was negotiating for the purchase of the shares of an investment banking house when that house, the Bank and the Trust Company failed. That was in November, 1930—a little more than a year after Banco began its financial career. In November, 1930 a receiver was appointed for the Bank and one for Banco. In February, 1931 the Comptroller of the Currency made an assessment on the shareholders of the Bank in the amount of $4,000,000 payable on or before April 1, 1931. And in March, 1931 the receiver of the Bank notified the stockholders of Banco that he had demanded payment of the assessment from the receiver of Banco and that he intended to proceed against them for collection of the assessment to the extent that he was unable to collect from Banco. In October, 1931 the receiver of the Bank brought an action against Banco as holder of substantially all of the Bank's shares. He obtained a judgment (*Keyes* v. *American Life Ins. Co.*, 1 F. Supp. 512) which was affirmed on appeal. *Laurent* v. *Anderson*, 70 F. 2d 819. Some $90,000 was paid on that judgment. The receiver of the Bank thereupon brought this suit against those stockholders of Banco who resided in the Western District of Kentucky in which he seeks to recover from each his proportionate part of the balance of the assessment. Similar suits against other stockholders were brought in federal district courts in other states. The District Court, after a trial, dismissed the bill. 32 F. Supp. 328. The Circuit Court of Appeals affirmed that judgment. 127 F. 2d 696. The case is here on certiorari.

I.

We are met at the outset with the contention that the decision in *Laurent* v. *Anderson*, *supra*, holding Banco liable on the assessment, is *res judicata* of the present claim; and that petitioner by bringing that suit made an election which bars the present action. We do not agree. Either the record owner or the actual owner of shares of a national bank may be liable on the statutory assessment.[6] *Richmond* v. *Irons*, 121 U. S. 27, 58; *Keyser* v. *Hetz*, 133 U. S. 138, 149; *Pauly* v. *State Loan & Trust Co.*, 165 U. S. 606; *Lantry* v. *Wallace*, 182 U. S. 536;

[6] Provisions for the termination of double liability on shares of national banks are contained in the Act of June 16, 1933, 48 Stat. 189, and the Act of August 23, 1935, 49 Stat. 708, 12 U. S. C. § 64a.

*Ohio Valley Nat. Bk.* v. *Hulitt*, 204 U. S. 162; *Early* v. *Richardson*, 280 U. S. 496; *Forrest* v. *Jack*, 294 U. S. 158. A receiver may sue both — partial satisfaction of the judgment against one being a *pro tanto* discharge of the other. *Ericson* v. *Slomer*, 94 F. 2d 437. And see *Continental Nat. Bank & Trust Co.* v. *O'Neil*, 82 F. 2d 650. The basis of liability of each is different — apparent or titular ownership in one case, actual or beneficial ownership in the other. Hence the issues involved in each suit are not the same.[7] See *Reconstruction Finance Corporation* v. *Pelts*, 123 F. 2d 503; *Reconstruction Finance Corporation* v. *Barrett*, 131 F. 2d 745, 748. If the receiver were barred from proceeding against one because he had already proceeded against the other, creditors of banks would be deprived of the full benefits of these statutes. The wisdom of the receiver's first suit rather than the fixed statutory liability would be the measure of their protection. There is no justification for such an impairment of the statutory scheme. The rules of election applicable to suits on contracts made by agents of undisclosed principals (*Pittsburgh Terminal Coal Corp.* v. *Bennett*, 73 F. 2d 387, 389) have been pressed upon us. But they have no application to suits to enforce a liability which has this statutory origin. Cf. *Christopher* v. *Norvell*, 201 U. S. 216, 225.

II.

The District Court found, and the Circuit Court of Appeals agreed, that Banco was organized in good faith and was not a sham; that it was not organized for a fraudulent purpose or to conceal enterprises conducted for the benefit of the Bank; that it was not a mere holding company; that it was not formed as a means for avoiding double liability on the stock of the Bank; and that the soundness of the Bank and its ability to meet the obligations could not be questioned until after the formation of Banco. Some of these findings have been challenged. But we do not stop to examine the evidence. We accept those findings, as they were concurred in by two courts and no clear error is shown. *Brewer Oil Co.* v. *United States*, 260 U. S. 77, 86; *Ala-*

[7] It is true that the court in Laurent v. Anderson, *supra*, stated that Banco was "in every sense the true and beneficial owner" of the shares of the Bank. 70 F. 2d p. 824. But it is apparent from the opinion that the court was answering the contention that the trustees of the participation certificates were responsible for the assessment. Banco's defense was based on § 63 of the National Bank Act. It argued that under that section only funds in the hands of the trustees were liable. That argument was rejected by the court.

*bama Power Co.* v. *Ickes*, 302 U. S. 464, 477. We conclude, however, that the courts below erred in dismissing the bill.

It is clear by reason of *Early* v. *Richardson, supra*, that if a stockholder of the Bank had transferred his shares to his minor children, he would not have been relieved from liability for this assessment. And see *Seabury* v. *Green*, 294 U. S. 165. That follows because of the policy underlying these statutes. One who is legally irresponsible cannot be allowed to serve as an insulator from liability, whether that was the purpose or merely the effect of the arrangement. A father who transfers his shares to his minor children has not found a substitute for his liability. See *Weston's Case*, 5 Ch. App. 614. It does not matter that the transfer was in good faith, without purpose of evasion and at a time when the bank was solvent. *Early* v. *Richardson, supra*. The vice of the arrangement is found in the nature of the transferee and his relationship to the transferor. Cf. *Nickalls* v. *Merry*, 7 Eng. & Irish App. 530. The same result will at times obtain where the transferee is financially irresponsible. This does not mean that every stockholder of a national bank who sells his shares remains liable because his transferee turns out to be irresponsible or impecunious. It is clear that he does not. *Earle* v. *Carson*, 188 U. S. 42, 54-55. But where after the sale he retains through his transferee an investment position in the bank, including control, he cannot escape the statutory liability if his transferee does not have resources commensurate with the risks of those holdings. In such a case he remains liable as a "stockholder" or "shareholder" within the meaning of these statutes to the extent of his interest in the underlying shares of the bank. For he retains control and the other benefits of ownership without substituting in his stead any one who is responsible for the risks of the banking business. The law has been edging towards that result. See *Hansen* v. *Agnew*, 195 Wash. 354; *Metropolitan Holding Co.* v. *Snyder*, 79 F. 2d 263; *Barbour* v. *Thomas*, 86 F. 2d 510; *Nettles* v. *Rhett*, 94 F. 2d 42. We think the result is necessary, lest the protection afforded by these double liability provisions be lost through transfers to impecunious or not fully responsible holding or operating companies whose stock is owned by the transferor. Whether the transfer is made in avoidance of the double liability as in *Corker* v. *Soper*, 53 F. 2d 190, or for business reasons which may be considered wholly legitimate, the result is the same. Depositors are deprived of the benefit of double liability in either event.

Thus it is no bar to the present suit that Banco was organized in good faith, that there was no fraudulent intent, that Banco was not a sham, that it was not a mere holding company, or that the shareholders of the Bank had no purpose of avoiding double liability. We are not concerned with any question of good intention. The question is whether the parties did what they intended to do and whether what they did contravened the policy of the law. By that test it is clear to us that the old stockholders of the Bank are liable. For they retained through Banco their former investment positions in the Bank, including control, and did not constitute Banco as an adequate financial substitute in their stead. Banco's asset position immediately after its sales of stock cannot be taken as the measure of its financial responsibility. Its liquid condition was fleeting; the raising of the cash was but an interim step in the planned evolution of Banco as a bank-stock holding company. It is the condition of Banco at the end of the promotion which is significant. Banco emerged as a bank-stock holding company. Technically it was not merely such a holding company as it had other interests and investments. But its main assets were stocks in banks, stocks which carried double liability. Its other assets—apart from the $25,000 of life insurance stock—were always highly suspect and dubious. In substance Banco as a going concern had no free assets which could possibly be said to constitute an adequate reserve against double liability on the bank stocks which it held. It was in no true sense comparable to an investment trust or holding company which holds bank stock in a diversified portfolio. If the small amount of life insurance stock be left out of account, the situation is in point of fact not materially different from the case where the only assets held were bank stocks carrying double liability. Such an arrangement, if successful, would allow stockholders of banks to retain all of the benefits of ownership without the double liability which Congress had prescribed. The only substitute which depositors of one bank would have for that double liability would be the stock in another bank carrying a like liability. The sensitiveness of one bank in the group to the disaster of another would likely mean that at the only time when double liability was needed the financial responsibility of the holding company as stockholder would be lacking. However that may be, the device used here can be so readily utilized in circumvention of the statutory policy of double liability that the stockholders of the holding company rather than the de-

positors of the subsidiary banks must take the risk of the financial success of the undertaking.[8]

That is a basis of liability sufficiently broad to include also the stockholders of Banco who had not been stockholders of the Bank. As we have noted, many of them acquired their shares either for cash or for shares in other banks. It must be assumed that in making those purchases or effecting those exchanges they knew what kind of an enterprise Banco was. See *Nettles* v. *Rhett*, *supra*, pp. 48-49; *Anderson* v. *Atkinson*, 22 F. Supp. 853, 863. Circulars of the Chicago Stock Exchange, on which Banco's shares were listed, gave a plain indication of the nature of the enterprise.[9] So did circulars of dealers.[10] And there would not seem

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8 The history of bank-stock holding companies shows that their organizers were acutely aware of this problem and at times took steps to protect the depositors of the subsidiary banks on possible assessments on the bank stocks. One holding company is said to have kept "at all times an amount in cash or its equivalent equal to our aggregate stockholders' liability on the bank stocks owned by us." Branch, Chain, and Group Banking, Hearings under H. Res. 141, 71st Cong., 2d Sess. (1930) p. 1181. A similar method was for the holding company "to carry in its treasury a large reserve of readily marketable securities which may be liquidated in order to make good any shareholders' liability that may be imposed upon the holding company." Bonbright & Means, The Holding Company (1932), p. 331. Cf. Nineteenth Annual Report, Superintendent of Banks of California (1928), p. 21. Another method of safeguarding the depositors was to make express provision in the charter of the holding company that its stockholders were ratably liable for any statutory liability imposed on it by reason of its ownership of bank stocks. Branch, Chain, and Group Banking, *op. cit.*, pp. 1042-1043; Barbour v. Thomas, 86 F. 2d 510, 513-514. Wisconsin provided for such a liability by statute. Wis. Stat. 1941, § 221.56.

9 "The BancoKentucky Company was organized under the laws of the State of Delaware on July 16, 1929, with an authorized capital of 2,000,000 shares of $10 par value. The Company was organized for the purpose of owning a controlling interest in state and national banks located primarily in Kentucky, Ohio and Indiana. Its charter gives it broad powers entitling it to engage in a wide range of investment and other activities.

"The BancoKentucky Company has acquired, through an exchange of stock, nearly 100% of the shares of the National Bank of Kentucky-Louisville Trust Company, and in addition its stockholders have subscribed to 480,000 shares of its stock for cash. This cash will be used for acquiring majority interests in other banks and for other corporate purposes."

In listing its shares on the Chicago Stock Exchange it gave the Exchange the following description of its business:

"(b) *Primary purpose:* To acquire control and operate Banks and Trust Companies.

(c) *Nature of Business:* This company has not engaged in the business of investing and reinvesting in a diversified list of securities of other corporations for revenue and profit, but has limited its activities to acquiring control of Banks and Trust Companies and the operation of same."

10 Thus a circular of Blyth & Co. stated:

"The Banco Kentucky Company was recently formed to acquire and hold controlling interests in commercial banks throughout the Middle West.

to be any doubt that the old stockholders of the Bank were given at the time of the exchange a fair picture of the nature of the enterprise which Banco was about to launch. Some shareholders of Banco claim the right to rescind their purchases of its shares on the ground of misrepresentations in the sale. But whether or not such relief might be granted in some instances, it seems clear that Banco's stockholders are bound by the decisions of the directors which determined, within the scope of the corporate charter, the kind and quality of the corporate undertaking. As was stated in *Christopher* v. *Brusselback,* 302 U. S. 500, 503, "A stockholder is so far an integral part of the corporation of which he is a member, that he may be bound and his rights foreclosed by authorized corporate action taken without his knowledge or participation. *Sanger* v. *Upton,* 91 U. S. 56, 58." And see *Pink* v. *A. A. A. Highway Express,* 314 U. S. 201, 207, and cases cited. The legality of the investments of Banco's funds for the most part is not challenged. It must be assumed that they were not *ultra vires.* They fall indeed into the category of acts of directors which normally cannot be challenged by stockholders. Cook, Corporations (8th ed.) § 684 These principles, basic in general corporation law, are relevant here as indicating that the stockholders of Banco cannot escape responsibility for the inadequacy of Banco's resources merely because the choice of its investments was made by the officers and directors—acts in which the stockholders did not participate and of which perhaps they had no actual knowledge. The fact that they may have claims against an officer or director for mismanagement does not relieve them from liability to the depositors of the subsidiary banks. Cf. *Scott* v. *DeWeese,* 181 U. S. 202, 213; *Lantry* v. *Wallace,* 182 U. S. 536, 548-554.

Normally the corporation is an insulator from liability on claims of creditors. The fact that incorporation was desired in order to

By charter, broad powers are conferred upon the Company, so that all types of operations in the financial field are permitted but no investments are contemplated other than controlling interests in financial institutions.

"Upon completion of present transactions the Company will control the National Bank of Kentucky, organized in 1834, the Louisville National Bank and Trust Co., organized 1884 as Louisville Trust Company, both of Louisville, Ky., the Pearl Market Bank & Trust Co., organized 1907, and the Brighton Bank & Trust Co., organized 1898, both of Cincinnati, Ohio, and the Central Savings Bank and Trust Company, organized 1906, of Covington, Ky. In addition, the Company has funds of approximately $6,000,000, which are expected to be used for the acquiring of additional banking institutions."

obtain limited liability does not defeat that purpose. *Elenkrieg v. Siebrecht,* 238 N. Y. 254. See 7 Harv. Bus. Rev. 496. Limited liability is the rule not the exception; and on that assumption large undertakings are rested, vast enterprises are launched, and huge sums of capital attracted. But there are occasions when the limited liability sought to be obtained through the corporation will be qualified or denied. Mr. Justice Cardozo stated that a surrender of that principle of limited liability would be made "when the sacrifice is essential to the end that some accepted public policy may be defended or upheld." *Berkey v. Third Ave. Ry. Co.,* 244 N. Y. 84, 95, *United States v. Milwaukee Refrigerator Transit Co.,* 142 Fed. 247. See Powell, Parent & Subsidiary Corporations (1931) pp. 77-81. The cases of fraud make up part of that exception. *Linn & Lane Timber Co. v. United States,* 236 U. S. 574; *Rice v. Sanger,* 27 Ariz. 15; *Donovan v. Purtell,* 216 Ill. 629, 640; *George v. Rollins,* 176 Mich. 144; *Higgins v. California, P. & A. Co.,* 147 Calif. 363. But they do not exhaust it. An obvious inadequacy of capital, measured by the nature and magnitude of the corporate undertaking, has frequently been an important factor in cases denying stockholders their defense of limited liability. *Luckenbach S. S. Co. v. Grace & Co.,* 267 Fed. 676, 681; *Oriental Inv. Co. v. Barclay,* 25 Tex. Civ. App. 543, 559, 64 S. W. 80, 88. And see *Weisser v. Mursam Shoe Corp.,* 127 F. 2d 344. Cf. *Pepper v. Litton,* 308 U. S. 295, 310; *Albert Richards Co. v. Mayfair, Inc.,* 287 Mass. 280, 288; *Erickson v. Minnesota & Ontario Power Co.,* 134 Minn. 209. That rule has been invoked even in absence of a legislative policy which undercapitalization would defeat. It becomes more important in a situation such as the present one where the statutory policy of double liability will be defeated if impecunious bank-stock holding companies are allowed to be interposed as non-conductors of liability. It has often been held that the interposition of a corporation will not be allowed to defeat a legislative policy, whether that was the aim or only the result of the arrangement. *United States v. Lehigh Valley R. Co.,* 220 U. S. 257; *Chicago, M. & St. P. Ry. Co. v. Minneapolis Civic & Commerce Assoc.,* 247 U. S. 490; *United States v. Reading Co.,* 253 U. S. 26. The Court stated in *Chicago, M. & St. P. Ry. Co. v. Minneapolis Civic & Commerce Assn., supra,* p. 501, that "the courts will not permit themselves to be blinded or ~~deceived by~~ mere forms or law" but will deal "with the substance of the

transaction involved as if the corporate agency did not exist and as the justice of the case may require." We are dealing here with a principle of liability which is concerned with realities not forms. As we have said, the net practical effect of the organization and management of Banco was the same as though the shares of the Bank were held in trust for beneficiaries who were in point of substance its only owners. Those who acquired shares of Banco did not enter upon an enterprise distinct from the banking business. Their investment in Banco was in substance little more than an investment in the shares of the Bank. They were as much in the banking business as any stockholder of the Bank had ever been. And they continued in that business through Banco which as a going concern lacked assets adequate as a reserve against the contingent statutory liability. Its stockholders were in point of substance the only source of funds available to satisfy the assessments. For these reasons the old group of stockholders must be held to have retained and the new group of stockholders must be held to have acquired liability as stockholders of the Bank.

To allow this holding company device to succeed would be to put the policy of double liability at the mercy of corporation finance. The fact that Congress did not outlaw holding companies from the national bank field nor undertake to regulate them during the period of Banco's existence can hardly imply that Congress sanctioned their use to defeat the policy of double liability. It is true that Congress later addressed itself to this problem and in the Banking Act of 1933 (48 Stat. 186, 12 U. S. C. § 61) established certain controls over them. In general, the Board of Governors of the Federal Reserve System was authorized to issue a voting permit entitling a holding company to vote the stock controlled by it on certain conditions. Apart from requirements for examination and non-affiliation with securities companies, § 19(a) and (e), certain standards for financial responsibility were established and holding companies seeking such permits were granted a specified period of time within which to meet those standards. Where the stockholders of the holding company were liable for the statutory liability, a specified reserve of readily marketable assets was required. § 19(c). Otherwise, the holding company was required to maintain free of any lien "readily marketable assets other than bank stock" in an amount equal to a larger percentage of the par value of the bank stocks owned. § 19(b). It is apparent

that Congress in that Act protected its policy of double liability by prescribing one standard of financial responsibility for holding companies whose shares were assessable by their terms and another for those whose shares were non-assessable.[11] We need not stop to consider what would be the measure of liability in cases arising under that Act where there had been no compliance with it. But if that Act had been applicable to Banco and Banco had complied with it, Banco would then have met the standards of financial responsibility which Congress had prescribed as adequate for the depositors. Yet the fact that Congress later wrote specific standards into the law means no more than a recognition on its part of an evil and a fashioning by it of a specific remedy. It can hardly mean that Congress by its earlier silence had sanctioned the use of the holding company to defeat the protection which it had provided for depositors of national banks. The legislative policy which Congress had long announced was the policy of double liability. It is that policy with which we are here concerned. It is that policy, declared by Congress, which the judicial power may appropriately protect in the way we have indicated, in absence of a choice by Congress of another method.

It is of course true that Delaware created this corporation. But the question of liability for these assessments is a federal question. The policy underlying a federal statute may not be defeated by such an assertion of state power. *Northern Securities Co.* v. *United States*, 193 U. S. 197, 349; *Seabury* v. *Green*, *supra*. The spectre of unlimited liability for stockholders has been raised. But there is no cause for alarm. Barring conflicting federal incorporation statutes, Delaware may choose such rules of limitation on the liability of stockholders of her corporations as she desires. And those laws are enforceable in federal courts under the rule of *Erie R. Co.* v. *Tompkins*, 304 U. S. 64. But no State may endow its corporate creatures with the power to place themselves above the Congress of the United States and defeat the federal policy con-

11 As stated in S. Rep. No. 77, 73d Cong., 1st Sess., p. 11: "The affiliates of this type (holding companies) are prohibited from voting the stocks of national banks unless they are willing to undertake to accept examination by the Federal Reserve Board, divest themselves of ownership of stock and bond financing concerns, and comply with regulations designed to insure their ownership of sufficient free assets to make sure that they can satisfy the double liability of their shareholders in case any of the banks owned by such a company should go into the hands of receivers or be closed."

cerning national banks which Congress has announced. We are concerned here with that problem and with that problem alone.

The result which we reach may be harsh to some of the stockholders of Banco. But rules of liability are usually harsh especially where they are not bottomed on fault. Thus private investors have frequently found contrary to their expectation or understanding that they purchased with their investment an unlimited liability for the debts of the enterprise. *Thompson* v. *Schmitt*, 115 Tex. 53; *Frost* v. *Thompson*, 219 Mass. 360; *Weber Engine Co.* v. *Alter*, 120 Kan. 557; *Rand* v. *Morse*, 289 Fed. 339. It has never been supposed, however, that the innocence and good faith of investors were barriers to such suits. *Horgan* v. *Morgan*, 233 Mass. 381, 385. Nor can we accede to the suggestion that those defenses should be available here. The policy underlying double liability is an exacting one. Its defeat cannot be encouraged through the utilization of financial devices which put a premium on ignorance.

The suggestion that there should be no liability without fault unless a statute establishes it denies the whole history of the judicial process in shaping the rules of vicarious liability. The liability of a master for the torts of his servant certainly started from no such foundation. And the rules which made those who purchased shares in Massachusetts business trusts responsible for the debts of the enterprise were evolved, with few exceptions, on a common law, not a statutory, basis. Magruder, The Position of Shareholders in Business Trusts, 23 Col. L. Rev. 423. In the field in which we are presently concerned, judicial power hardly oversteps the bounds when it refuses to lend its aid to a promotional project which would circumvent or undermine a legislative policy. To deny it that function would be to make it impotent in situations where historically it has made some of its most notable contributions. If the judicial power is helpless to protect a legislative program from schemes for easy avoidance, then indeed it has become a handy implement of high finance. Judicial interference to cripple or defeat a legislative policy is one thing; judicial interference with the plans of those whose corporate or other devices would circumvent that policy is quite another. Once the purpose or effect of the scheme is clear, once the legislative policy is plain, we would indeed forsake a great tradition to say we were helpless to fashion the instruments for appropriate relief.

In summary, we see no difference between the various classes of stockholders of Banco which would support a difference in their liability. Those who purchased stock of Banco for cash were as much participants in the banking business as those who acquired their stock in exchange for shares of the Bank. Together they shared the benefits of ownership of the subsidiary banks, including control. Certainly a sale of shares of Banco by the old stockholders of the Bank did not give those shares an immunity bath. To draw distinctions between the classes of stockholders of Banco would be to make the protection afforded by these statutes turn on accidents of acquisition quite irrelevant to the concept of "stockholders" or "shareholders" on whom Congress placed this liability. One simple illustration will make that plain. A purchases shares of an underlying bank for $10,000 in cash and exchanges those shares for shares of Banco. B hands over to Banco $10,000, Banco purchases the shares of the underlying bank, and then issues its shares to B. From the practical point of view A and B are investors of the same class. To say that A is liable and B not liable when both start with cash and end with identical investments is to make the difference between liability and no liability turn on distinctions which have no apparent relevancy to the legislative policy which the rule of double liability was designed to protect. And to say that courts may hold A liable but not B is to make the occasions for the assertion of judicial power turn on whimsical circumstances.

The final suggestion is that the old stockholders of the Bank remain liable for the full assessment on the shares of the Bank which they exchanged for shares of Banco. But that overlooks the fact that their interest in those underlying shares was diluted by the issuance of Banco's shares to others.[12] Double liability is an incidence of ownership. It has long been held that a stockholder who in good faith parts with all his interest in the shares rids himself of that double liability, even though his transferee is not responsible. *Earle* v. *Carson, supra.* We could hardly adhere to that principle and still hold the old stockholders of the Bank

12 The old stockholders of the Bank have a lesser interest in the shares of the Bank than they had prior to the exchange. Their interest in the shares of the Bank decreased proportionately with the increase in the outstanding stock of Banco. That resulted in a *pro rata* reduction in their liability. The other group of stockholders of Banco acquired that portion of the liability of which the old stockholders of the Bank were relieved.

liable for the full assessment on the shares which they exchanged for shares of Banco. The other stockholders of Banco acquired through their investment in it an interest in the shares of the Bank. To the extent of that interest the beneficial ownership of the old stockholders of the Bank in its shares was as definitely reduced as if they had made a transfer of that part of their holdings.

Certain stockholders of Banco claim that they are entitled to rescind their purchases of Banco's shares because of misrepresentations made to them when they acquired the shares. We do not reach those questions. Nor do we stop to determine whether such a defense would avoid liability on the assessment (cf. *Oppenheimer* v. *Harriman Nat. Bank & Trust Co.*, 301 U. S. 206) and, unlike the case where some shareholders are insolvent (*United States* v. *Knox*, 102 U. S. 422, 425), increase the *pro rata* liability of the other shareholders of Banco. It is sufficient at this time to state that the liability of the shareholders of Banco would be measured by the number of shares of stock of the Bank, whether several or only fractional, represented by each share of stock of Banco; and that the assessment liability of each share of stock of Banco would be a like proportion of the assessment liability of the shares of the Bank represented by the former.

The judgment of the Circuit Court of Appeals is reversed and the cause is remanded to the District Court for proceedings in conformity with this opinion.

*Reversed.*

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Mr. Justice Jackson, dissenting.

Mr. Justice Roberts, Mr. Justice Reed, Mr. Justice Frankfurter, and I find ourselves unable to join in the judgment of the Court.

The Court accepts concurrent findings of fact by the two lower courts, but reverses their concurrent judgment. It holds that the findings establish liability as matter of law on two very different kinds of stockholdings: (1) holding company stock taken in exchange for double liability stock of the National Bank of Kentucky; and (2) holding company stock bought and fully paid for in cash. We think holders of the latter are not liable on any principle heretofore known to the law and that if owners of

the former are to be held it must be on a quite different principle than that stated by the Court.

I.

Former National Bank of Kentucky stockholders had stock in the Bank itself which carried double liability.[1] The Bank failed November 30, 1930; and if they had then held that stock, each would have been liable for assessment upon his shares. The aggregate assessment was $4,000,000. Only about a year before the failure, on September 19, 1929, this double-liability bank stock was exchanged for shares of the holding company purporting to be fully paid and nonassessable. At the same time Bank of Kentucky stockholders also bought additional holding company stock for cash to the amount of $4,471,950. Bank of Kentucky stockholders as a group thus paid into the holding company cash more than sufficient to meet the assessment now levied. In addition to that, investors who were not connected with the Bank bought shares for cash amounting to $5,397,000. The Court nevertheless holds that the Bank of Kentucky stockholders contravened the policy of the law and are subject to the double liability because they "did not constitute Banco as an adequate financial substitute in their stead." We do not see how such a statement of fact, and it certainly is not a matter of law, can be conformable with acceptance of the findings of fact of the courts below. Nor are we able to reconcile the view that "the old group of stockholders must be held to have retained . . . the *liability as stockholders of the bank*" with the one later expressed that their interest was "diluted" so as to give them a *pro rata* reduction of liability. (See

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[1] The pertinent sections of the Bank Act follow:

"The shareholders of every national banking association shall be held individually responsible . . . for all contracts, debts, and engagements of such association, to the extent of the amount of their stock therein, at the par value thereof, in addition to the amount invested in such shares; . . ." 12 U. S. C. § 63.

"The stockholders of every national banking association shall be held individually responsible for all contracts, debts, and engagements of such association, each to the amount of his stock therein, at the par value thereof in addition to the amount invested in such stock. The stockholders in any national banking association who shall have transferred their shares or registered the transfer thereof within sixty days next before the date of the failure of such association to meet its obligations, or with knowledge of such impending failure, shall be liable to the same extent as if they had made no such transfer, to the extent that the subsequent transferee fails to meet such liability; but this provision shall not be construed to affect in any way any recourse which such shareholders might otherwise have against those in whose names such shares are registered at the time of such failure." 12 U. S. C. § 64.

note 12 of the opinion of the Court.) [Emphasis supplied.] It seems to us that the transfer of their bank stock to the holding company either was valid, in which case it relieved of all liability; or it was invalid, in which case it relieved of no liability. The doctrine that a transfer may be good enough to dilute liability but bad enough to carry along a part of it is new to us and we have difficulty grasping its implications.

We are, however, agreed that it would be a proper use of the power of this Court for it to examine the evidence that lies back of these findings and determine whether clear error has been committed and whether the conditions disclosed are such that a *bona fide* transfer of the stock took place sufficient to shake off double-liability obligations.

In spite of the exchange of National Bank of Kentucky stock, its stockholders through the holding company kept both a large measure of control of the Bank and the benefits of investment in it. They, or those acting in their behalf, had determined the policy of the holding company, had sponsored its representatives, and had selected its officers and personnel, including the manager who proved to be false to his trust. There is evidence that the National Bank of Kentucky had for some time been under criticism by the Comptroller for many of its loans and some of its policies, although it is found not to have been insolvent. The exchange did not consist of individual acts but was a concerted movement, planned by the Bank management, by which the holding company absorbed all of the stockholdings and all of the double liability.

The Court might properly, if examination of the evidence should warrant it, reach a legal conclusion that the double liability of the stockholders of the National Bank of Kentucky survives the exchange and that those who have continued their interest in the Bank through the holding company are liable upon assessment in the same manner and to the extent that they would have been had the holding company transactions never occurred. But this would be because the formal transfer of the stock out of their own names would not be recognized as a defense. The Court's conclusion rests on a quite different theory. It concludes that the transfer was valid to relieve these stockholders of their liability *as stockholders of the Bank*, but that they became subject to a new and smaller liability *as stockholders of a holding company*. With this we cannot agree.

The holding company, its financing, its management, and all that relates to it constitute relevant material as to whether under principles that have long been recognized the transfer is good. We do not think they create a new liability.

## II.

After holding that former owners of National Bank of Kentucky shares are liable because they did not find an adequate substitute for their own personal liability, the Court proceeds to hold purchasers of holding-company stock for cash to be under a substituted liability *pro tanto*. The grounds upon which Bank of Kentucky stockholders and non-Bank of Kentucky stockholders are both held seem to conflict. If the new stockholders for cash are liable it is hard to see why the old ones have not found a substitute, and if the Bank of Kentucky stockholders have not found a substitute, it is difficult to see a basis on which the new stockholders are liable.

Stock purchasers for cash have at no time owned a stock that purported to carry double liability. On the contrary, by the terms of the stock certificates and by the law of the corporation's being, their shares were fully paid and nonassessable. These stockholders cannot be said in any way to have assumed any express or implied contractual assessment liability. No statute of the United States and no applicable state statute then or since has purported to impose a double liability upon these holding-company shares. No controlling precedent in this Court at the time these stockholders purchased or since (until today) purported to attach a double liability to such shares.[2]

[2] The authorities cited to support the Court's disregard of the corporate entity fall far short of persuasion. The quotation of the statement by Mr. Justice Cardozo from Berkey v. Third Avenue Railway Co., 244 N. Y. 84, "that a surrender of that principle of limited liability would be made 'when the sacrifice is essential to the end that some accepted public policy may be defended or upheld' " has a very different significance in its context. The facts, including interchangeable names of parent and subsidiary, complete financial and operating domination, and use of one company's assets by the other, indicated a stronger case for disregard of the corporate fiction than do the findings here. Nevertheless, Chief Judge Cardozo considered that the corporate entity could not be disregarded in favor of a tort claimant and said: "In such circumstances, we thwart the public policy of the State instead of defending or upholding it, when we ignore the separation between subsidiary and parent, and treat the two as one."

Other cases cited afford no more support for the decision. United States v. Milwaukee Refrigerator Transit Co., 142 F. 247, held that payments by a carrier to a corporation wholly controlled by a shipper

The reason given for this decision is that "the interposition of a corporation will not be allowed to defeat *a legislative policy*" and that "no State may endow its corporate creatures with the power to place themselves above the Congress of the United States and defeat the *federal policy concerning national banks which Congress has announced.*" [Italics supplied.]

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might constitute rebates under the Elkins Act. The statements in Powell, Parent & Subsidiary Corporations, 77-81, are completely general and to be read in the light of the specific categories which precede the page citation, all of which involve active wrong by a parent corporation. Linn & Lane Timber Co. v. United States, 236 U. S. 574, involved the question whether an "instrumentality" corporation could acquire rights which would enable it to stand better than its transferor-creator. Rice v. Sanger Bros., 27 Ariz. 15, found a corporation to be organized for fraudulent purposes and the former partners who became its stockholders were held liable. Donovan v. Purtell, 216 Ill. 629, holds nothing more than that an officer of a corporation who is personally guilty of fraud will be held liable therefore. George v. Rollins, 176 Mich. 144, stands for the proposition that equity will enforce a restrictive covenant against a successor corporation formed for the purpose of evading it. Higgins v. California Petroleum Co., 147 Cal. 363, held that in the circumstances certain successor corporations assumed a lease and therefore had to pay royalties; there was no disregarding of the corporate entity involved. Luckenbach S.S. Co. v. Grace & Co., 267 F. 676, comes nearer the mark, but still is far wide of it. A steamship corporation leased its fleet of vessels to a $10,000 corporation, formed and 90 per cent owned by it, for an utterly inadequate rental. It was held that this turning over of the corporation's ships to a subsidiary which was "itself in another form" rendered the parent corporation liable for the subsidiary's breach of contract. Oriental Investment Co. v. Barclay, 25 Tex. Civ. App. 543, allowed a hotel employee to recover for personal injuries against the parent holding company, even though technically he was the employee of the subsidiary operating company, of whose existence he was unaware and which had been capitalized with $2,000 to operate a property whose monthly rental alone was $1500. Weisser v. Mursam Shoe Corp., 127 F. 2d 344, arose on dismissal of the complaint and it was held that on a full trial it might be found that the subsidiary was "only a tool of the other defendants, deliberately kept judgment proof, to obtain the benefits of a lease with plaintiffs without assuming any obligations. The plaintiffs allege that this was done fraudulently. . . ." Pepper v. Litton, 308 U. S. 295 and Albert Richards Co. v. Mayfair, Inc., 287 Mass. 280, both dealt with cases where parent corporations claimed priority over other creditors of a subsidiary; in each, the subsidiary was held to be an instrumentality of the parent and, to avoid a fraud on creditors, the latter's claim of priority was denied. In Erickson v. Minnesota & Ontario Power Co., 134 Minn. 209, a parent corporation was held liable for damage caused by a dam owned by a subsidiary; the parent paid the operating expenses of the dam, took all the earnings of the subsidiary, had a mortgage on all its assets, and in addition had a direct right of control over the operation of the dam. United States v. Lehigh Valley Railroad, 220 U. S. 257, and United States v. Reading Co., 253 U. S. 26, held that a railroad's exercise of its power as a stockholder might amount to such a commingling of affairs as to make it liable for a violation of the commodities clause. Chicago, Milwaukee & St. Paul Ry. Co. v. Minneapolis Civic Association, 247 U. S. 490, held that additional terminal charges made by a wholly owned subsidiary as compared with terminal charges by the parent might be held to constitute a discrimination.

We have been unable to find that Congress ever has announced a legislative policy such as the Court announces. And the Court nowhere points it out. The National Banking Act applicable at the time provided that the stockholders "of every national banking association" shall be under assessment liability. But Congress nowhere has said that the stockholders of a corporation that is not a national banking association shall be liable to assessment because the latter corporation held some or all of the stock of a national bank. Indeed, the history of banking legislation shows that Congress has considered the problems created by the holding company and not only has failed to adopt such a policy as the Court is declaring, but has made other provisions inconsistent with such a policy.

No legislation on the subject appears until 1933, when Congress enacted detailed regulation of the relations between holding companies and national banks. It required the holding company to obtain a permit to vote national bank shares and empowered the Board of Governors of the Federal Reserve System to grant or withhold the permit.[3] No permit can be granted except upon

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[3] § 19 of the Banking Act of 1933, amending § 5144 of the Revised Statutes, provides in part as follows:

". . . shares controlled by any holding company affiliate of a national bank shall not be voted unless such holding company affiliate shall have first obtained a voting permit as hereinafter provided, which permit is in force at the time such shares are voted.

. . . . . .

"For the purposes of this section shares shall be deemed to be controlled by a holding company affiliate if they are owned or controlled directly or indirectly by such holding company affiliate, or held by any trustee for the benefit of the shareholders or members thereof.

"Any such holding company affiliate may make application to the Federal Reserve Board for a voting permit entitling it to cast one vote at all elections of directors and in deciding all questions at meetings of shareholders of such bank on each share of stock controlled by it or authorizing the trustee or trustees holding the stock for its benefit or for the benefit of its shareholders so to vote the same. The Federal Reserve Board may, in its discretion, grant or withhold such permit as the public interest may require. In acting upon such application, the Board shall consider the financial condition of the applicant, the general character of its management, and the probable effect of the granting of such permit upon the affairs of such bank, but no such permit shall be granted except upon the following conditions:

"(a) Every such holding company affiliate shall, in making the application for such permit, agree (1) to receive, on dates identical with those fixed for the examination of banks with which it is affiliated, examiners duly authorized to examine such banks, who shall make such examinations of such holding company affiliate as shall be necessary to disclose fully the relations between such banks and such holding company affiliate and the effect of such relations

certain conditions, and assumption by holding-company stockholders of an assessment liability is not among them. In general, they are (a) that the holding company must submit to examination in the same manner as the national bank and must publish periodic statements of condition; (b) that after five years from the statute's enactment, each holding company must possess readily marketable assets and free assets other than bank stock in a prescribed amount; and (c) that after five years a holding company *whose stockholders or members are individually and severally liable* may be relieved of establishing a part of this reserve under certain circumstances. Congress was informed that some bank stock holding corporations were, by the law of the states in which they were incorporated, subject to double liability just as were stockholders

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upon the affairs of such banks, such examinations to be at the expense of the holding company affiliate so examined; (2) that the reports of such examiners shall contain such information as shall be necessary to disclose fully the relations between such affiliate and such banks and the effect of such relations upon the affairs of such banks; (3) that such examiners may examine each bank owned or controlled by the holding company affiliate, both individually and in conjunction with other banks owned or controlled by such holding company affiliate; and (4) that publication of individual or consolidated statements of condition of such banks may be required;

"(b) After five years after the enactment of the Banking Act of 1933, every such holding company affiliate (1) shall possess, and shall continue to possess during the life of such permit, free and clear of any lien, pledge, or hypothecation of any nature, readily marketable assets other than bank stock bank stocks controlled by such holding company affiliate, which amount shall in an amount not less than 12 per centum of the aggregate par value of all be increased by not less than 2 per centum per annum of such aggregate par value until such assets shall amount to 25 per centum of the aggregate par value of such bank stocks; and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum on the book value of its own shares outstanding until such assets shall amount to such 25 per centum of the aggregate par value of all bank stocks controlled by it;

"(c) Notwithstanding the foregoing provisions of this section, after five years after the enactment of the Banking Act of 1933, (1) any such holding company affiliate the shareholders or members of which shall be individually and severally liable in proportion to the number of shares of such holding company affiliate held by them respectively, in addition to amounts invested therein, for all statutory liability imposed on such holding company affiliate by reason of its control of shares of stock of banks, shall be required only to establish and maintain out of net earnings over and above 6 per centum per annum on the book value of its own shares outstanding a reserve of readily marketable assets in an amount of not less than 12 per centum of the aggregate par value of bank stocks controlled by it, and (2) the assets required by this section to be possessed by such holding company affiliate may be used by it for replacement of capital in banks affiliated with it and for losses incurred in such banks, but any deficiency in such assets resulting from such use shall be made up within such period as the Federal Reserve Board may by regulation prescribe . . . ." June 16, 1933, c. 89, 48 Stat. 186-7.

of banks. It was also informed that other bank holding corporations by the law of their incorporation were not so liable.[4] It did

[4] At the Senate hearings which preceded the Banking Act of 1933, Mr. L. E. Wakefield, vice-president of one of the largest bank holding companies, testified as follows with respect to double liability:

"Mr. Wakefield. The stockholders of the First Bank Stock Corporation, being a Delaware corporation, do not have a double liability. When we started to organize this institution we did all the work on the theory we would have it a Minnesota corporation, which would have double liability. At the last minute, when we found that every stockholder in North Dakota, South Dakota, and Montana would, in case of death, have a double inheritance tax, they complained so strongly about that situation we shifted and put it into a Delaware corporation.

* * * * *

"The other factor that we have heard discussed and that I think of in connection with banking such as we are doing is this thought in the public mind, or some minds, that, for instance, our being a Delaware corporation was intended to avoid the double liability of stockholders. I would say that if that is of importance it might be easily provided that a holding company should create a surplus account in its holdings or build up a surplus account of some proportion of the capital of the banks that should be kept in liquid securities, or something of that sort. . . ." Hearings before Senate Committee on Banking and Currency Pursuant to S. Res. 71, 71st Cong., 3d Sess., Pt. 4, pp. 616, 620.

Earlier, Mr. J. W. Pole, Comptroller of the Currency, had testified:

"Mr. Pole. We call that a group banking system in the Northwest. In the case of the Northwest and the First Bank Stock Corporation, I think that their stock is not subject to the double liability, although the stock of some holding corporations is subject to double liability. But in the case of those two corporations, in those particular cases—not that it obtains too generally—they have invested in securities other than bank stocks, so that a judgment against either one of those corporations would be good for the assessment.

Mr. Willis. In those particular cases?

Mr. Pole. In those particular cases; yes, sir.

Mr. Willis. But there are cases where they are not subject to the assessment?

Mr. Pole. There are cases where they are not subject to the assessment; yes, and where they hold nothing but bank stocks.

Mr. Willis. In those cases where you have an affiliated bank that buys all the stock of the bank itself, what becomes of the double liability of the shareholder?

Mr. Pole. The securities company where it buys the stock of the bank itself, would be the holder of the stock and subject to assessment.

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Mr. Willis. Is not the double liability then very largely neutralized?

Mr. Pole. Yes.

Mr. Willis. What have you done to correct that?

Mr. Pole. We have done nothing to correct it.

Mr. Willis. What can be done by law to correct it?

Mr. Pole. That is a big problem.

Mr. Willis. Can you make a recommendation covering that along with your other problems?

Mr. Pole. Yes."

Senate Hearings, *supra*, Part 1, pp. 27-28.

For a provision extending double liability to holding company stockholders, see Wisconsin Stat. (1943) §221.56(3).

not expressly or by implication recognize or create a uniform double liability by federal act on stockholders of state-created holding companies. It made specific provision, on the contrary, for each class of corporation. Where does this Court get authority to disregard the distinction Congress has thus created and to impose a single rule of its own making instead? When Congress has expressly set up a standard of diversification for holding company assets and has given the companies five years to meet it, from what do we derive authority to say the five-year adjustment period shall be ignored? How can we say retroactively that there is a liability for failure to do before Congress acted something which, after it did act, it expressly gave five years to do? And how can such a result be said to be an enforcement of congressional policy, which we understand to be the basis of the Court's opinion?

## III.

If to legislate were the province of this Court, we would be at liberty candidly to exercise discretion toward the undoing of the holding company. Some of us feel that as utilized in this country it is, with a few exceptions, a menace to responsible management and to sound finance, shifting control of local institutions to absentee managements and centralizing in few hands control of assets and enterprises bigger than they are able well to manage—views which are matters of record.[5]

But we are of one opinion that no such latitude is confided to judges as here is exercised. We are dealing with a variety of liability without fault. The Court is professing to impose it, not as a matter of judge-made law, but as a matter of legislative policy, and it cannot cite so much as a statutory hint of such a policy. The Court is not enforcing a policy of Congress; it is competing with Congress in creating new regulations in banking, a field peculiarly within legislative rather than judicial competence. Nor was such a policy of assessment liability one whose importance was so transcending as to set aside the policy of permitting corporate enterprise under limited liability. Congress has since repealed the

[5] See 56 Reports of American Bar Association (1931) p. 763; Briefs for Government in Electric Bond & Share Co. v. S. E. C., 303 U. S. 419; testimony in support of a proposal to withdraw from holding companies tax exemption of intercorporate dividends, Hearings before Senate Committee on Finance, on H. R. 8974, 74th Cong., 1st Sess., p. 221, *et seq.*

double liability, even of holders of stock in national banks;[6] and when in force, it had little practical value to depositors.[7] States also have abandoned the assessment plan.[8] Courts should, of course, see that the congressional policy is not defeated by any fraud, by creating sham corporations, or by any other artifice. When, however, assessment liability is a failure only because the corporate owner of the stock is not solvent, that is not a circumstance which will warrant disregard of the corporate entity so as to render stockholders liable. The findings here, accepted by the Court, eliminate every charge of fraud, bad faith, or intentional evasion of liability.[9]

We are fully agreed that Bank of Kentucky depositors, however, should not be prejudiced by a transfer to the holding company of its stock in violation of letter or spirit of the National Banking Act. If the case warrants disregard of the transfer, the depositors then would have just the protection that they would have enjoyed had no holding company intervened. The Court,

6 June 16, 1933, c. 89, § 22, 48 Stat. 189, Aug. 23, 1935, c. 614, § 304, 49 Stat. 708; 12 U. S. C. § 64a.

7 Comptroller Pole stated at the Senate hearings: "We hear a good deal about double liability. It is not so important as at first one might so regard it. As an illustration, the deposits, we will say, of a bank with $100,000 capital would be ordinarily $1,000,000. If you collected the entire 100 per cent assessment, you would only collect 10 per cent of your deposits after all. . . . But in practice you would not collect over 50 per cent of that. We do collect, as a matter of fact, just about 50 per cent." Hearings, *supra* note 4, Pt. 1, p. 28.

Depositors in the bank have already received 77 per cent of their deposits. Few pre-depression investments have yielded so much. About 6,000 stockholders of Banco have lost 100 per cent of their investment, and are now faced with liability in undetermined amounts. As to many of them, it is idle to say that they had actual responsibility for the Bank's management or any better knowledge of its affairs than the depositors.

8 Within the last decade at least thirty-one states which formerly had double liability have abolished it either absolutely or upon compliance with certain conditions. Only five states appear to have retained their double liability provisions intact, and in one of these a proposal to abolish it is currently being considered. See "Stockholders' Double Liability," Commerce Clearing House State Banking Law Service, Vol. II.

9 Findings of the trial court included the following:

"61. Banco was organized in good faith.

62. Banco was 'certainly not a sham.'

63. Banco was 'not organized for a fraudulent purpose or to conceal secret or sinister enterprises conducted for the benefit of the Bank.'

64. Banco was not a mere holding company.

65. Banco 'was formed for the purpose set out in the letter of July 19, 1929, and for no other purpose.'

66. Banco 'was not formed as a medium or agency through which to avoid double liability on the stock of the Bank.'"

The removal of liability is conditioned upon giving the notice prescribed.

however, makes the holding company a windfall to bank creditors by extending the liability to persons never otherwise reachable. We may disallow the holding company as a sanctuary for stockholders escaping pre-existing liability without making of it a trap for unwary and unwarned investors.

To disregard the transfer of this stock, and to hold former stockholders liable to the same extent as if they had made no such transfer, is the manner of proceeding indicated under proper circumstances by the National Banking Act itself. Instead of considering whether to disregard the transfer the Court disregards the corporate entity of the holding company because it says these obligations arise from legislative policy. Even if we could find such a policy, legislative liabilities are numerous. It is probably a legislative policy that a corporation shall pay all of its debts. The reasoning employed by the Court, we should think, would leave it uncertain whether stockholders may not be liable for many other types of indebtedness. Congress, if the matter of banking reform were left to it, could define the limits of vicarious liability at the time it was imposed. The Court is leaving the limits and extent of that liability so vague that a whole cluster of decisions will have to be written to clarify what is being done today. And meanwhile we know of no way that a stockholder can learn the extent and circumstances of stockholder liability except to give his name to a leading case.[10]

The Court admits that the judgment is "harsh." Why is it so if it is according to any law that was known or knowable at the time of the transactions? To enforce a double liability so incurred would be no harsher than to enforce any contract obligation that had been assumed without expecting it would result in liability. This decision is made harsh by the element of surprise.[11] Its only harshness is that which comes of the Court's doing with backwards effect what Congress has not seen fit to do with forward effect.

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[10] This Court has considered the disregard of the corporate fiction in Donnell v. Herring-Hall-Marvin Safe Co., 208 U. S. 267, 273 and Klein v. Board of Supervisors, 282 U. S. 19, 24.

[11] In authoritative studies made prior to the origin of this controversy which included studies of many of the cases cited by the Court's opinion we are unable to find a trace or suggestion of the present theory of stockholder liability for corporate obligations created by legislation. See Douglas and Shanks, Insulation from Liability through Subsidiary Corporations," (1929) 39 Yale L. J. 193; Powell, Parent and Subsidiary Corporations (1931), esp. Ch. III; Wormser, Disregard of the Corporate Fiction (1927).